Issued
July 30, 2018

DISTRICT OF COLUMBIA COURT OF APPEALS
BOARD ON PROFESSIONAL RESPONSIBILITY

In the Matter of:	:	
	:	
JONATHAN C. DAILEY,	:	Board Docket No. 16-BD-071
	:	Bar Docket Nos. 2015-D104 &
Respondent.	:	2015-D246
	:	
A Member of the Bar of the	:	
District of Columbia Court of Appeals	:	
(Bar Registration No. 448141)	:	

REPORT AND RECOMMENDATION OF THE
BOARD ON PROFESSIONAL RESPONSIBILITY

Respondent Jonathan C. Dailey is charged in a four-count Specification of Charges with violating District of Columbia Rule of Professional Conduct ("Rule") 1.7(b)(4) (personal interest conflict) in a matter in which he represented Tabitha Fitzgerald (Count I). The Specification also charges Respondent with violating Rules 1.15(a), (c), and (d) (intentional misappropriation, failing promptly to notify or render a full accounting, and failing to keep disputed funds in an escrow account) arising out of his litigation funding agreement with Lawsuit Financial Corporation ("LFC") (Count II). The Specification further charges violations of Rules 1.15(a), (c), and (d) (reckless misappropriation and failing promptly to deliver funds) in a personal injury case Respondent handled for John Mack (Count III). Finally, Respondent is charged with violating Rule 1.15(a) (commingling and incomplete record-keeping) (Count IV).

The Ad Hoc Hearing Committee found clear and convincing evidence that Respondent committed all of the charged Rule violations. Because it found

intentional misappropriation and reckless misappropriation in Counts II and III respectively, the Committee recommended that Respondent be disbarred pursuant to *In re Addams*, 579 A.2d 190, 191 (D.C. 1990) (en banc).

Disciplinary Counsel takes no exception to the Hearing Committee's Report and Recommendation. Respondent takes exception to its findings, conclusions, and recommended sanction. First, Respondent contends that the Hearing Committee's finding of a Rule 1.7(b)(4) violation in Count I was wrong because he did not charge his client Tabitha Fitzgerald a fee and because she implicitly consented to the conflicted representation. With respect to Count II, Respondent argues that the strictures of Rule 1.15 do not apply to his relationship with LFC, a commercial litigation-funding firm. Finally, as to Count III, Respondent contends he did not recklessly misappropriate funds or fail to make prompt payment to a medical provider. Respondent does not take exception to the Hearing Committee's finding of commingling and incomplete record-keeping in Count IV.

Having considered the record, the parties' briefs, and the oral argument, we concur with the Hearing Committee's factual findings as supported by substantial evidence in the record, supplemented by our own factual findings for which we cite directly to the record (*see* Board Rule 13.7). We agree that Respondent recklessly misappropriated entrusted funds in violation of Rule 1.15(a) in the Mack matter (Count III) and accordingly recommend that Respondent be disbarred.[1]

[1] Because the additional violations of Rule 1.15(c) and Rule 1.15(d) in the Mack matter do not affect the sanction given the proven reckless misappropriation, we address those charges only briefly. *See infra*, at n.4. We recommend that the Court also adopt the Hearing Committee's

We also concur in the Hearing Committee's finding of a violation of Rule 1.7(b)(4) in the Fitzgerald matter (Count I), but clarify that Disciplinary Counsel had the burden of proving the absence of informed consent once consent was raised as a defense by Respondent.

Finally, we discuss – but do not adopt – the Hearing Committee's conclusion that Rule 1.15 should apply to an alternative litigation-financing arrangement, in which an attorney undertakes a non-recourse obligation to pay a third-party lender a percentage of the fees that he recovers in a contingent fee representation. The substantive law relating to such arrangements is undeveloped, and the application of disciplinary misappropriation principles to such commercial arrangements raises weighty policy questions. Because we recommend Respondent's disbarment on unrelated grounds, those complicated issues need not be resolved in this case. We therefore decline to find violations of Rules 1.15(a), (c), and (d) in the LFC matter (Count II).

A. Count I: Conflict of Interest (Fitzgerald)

Rules 1.7(b)(4) and (c)(1) provide, in pertinent part, that a lawyer "shall not represent a client with respect to a matter if . . . [t]he lawyer's professional judgment on behalf of the client will be or reasonably may be adversely affected by the lawyer's . . . own financial, business, property, or personal interests" unless the client "provides informed consent to such representation after full disclosure of the

finding of the Rule 1.15(a) (commingling and failing to keep complete records) violation in Count IV, to which neither party takes exception.

existence and nature of the possible conflict and the possible adverse consequences of such representation." Even with the consent of a client, a representation is nevertheless proscribed unless the lawyer "reasonably believes" he will be able to provide "competent and diligent representation." *See* Rule 1.7(c)(2). Here, Disciplinary Counsel argued, and the Hearing Committee found, that Respondent did not obtain his client's informed consent to the conflicted representation. Moreover, under the facts of this case the conflict was so fundamental that it was non-consentable.

Rule 1.0(e) defines "informed consent" as "the agreement by a person to a proposed course of conduct after the lawyer has communicated adequate information and explanation about the material risks of and reasonably available alternatives to the proposed course of conduct." In this case, Respondent purchased a condominium unit in Georgetown in 1996 and later sold it to a third-party with an option to repurchase. FF 3, 8.[2] Beginning in 2003 or 2004, Respondent had a romantic relationship with Tabitha Fitzgerald. FF 10. In 2007, Respondent decided to repurchase the unit, but could not qualify for a mortgage. FF 9, 11. Respondent thus arranged for Ms. Fitzgerald to take title to the condominium, but committed personally to pay the mortgage, condominium fees, assessments, and real estate taxes while he lived there. FF 12, 14. The purchase closed in March 2007, and a month later Ms. Fitzgerald did a "cash-out" refinancing pursuant to which

[2] The Hearing Committee's Findings of Fact are cited as "FF_." The Hearing Committee Report and Recommendation is cited as "HC Rpt."

Respondent "kept tens of thousands of dollars." FF 13. Because she was obligated on the mortgage loans, Ms. Fitzgerald and Respondent agreed that he would exercise his option to re-purchase the condominium unit within "a year or two." FF 14.

By 2010 or early 2011, the romance had ended, and Respondent had stopped paying the mortgage and assessments. FF 15. Ms. Fitzgerald first learned about his default when she received a foreclosure notice from the Condominium Association. FF 16. On May 25, 2011, the Association sued her in Superior Court to recover the unpaid assessments and to foreclose on the unit. *Id.*

Respondent undertook to represent Ms. Fitzgerald in the matter and filed an answer to the complaint on her behalf in July 2011. FF 17.

Respondent did not advise Ms. Fitzgerald that his interests in the subject matter of the lawsuit were adverse to hers. He did not advise her to consult with another attorney about the propriety of his representation. FF 21. He did not make any written disclosures to her about conflicts of interest and did not advise her that she had a right to bring a third-party claim against him. FF 20-21. In fact, Respondent never raised the conflict issue with Ms. Fitzgerald because he claimed that he "never even thought about" the possibility that his personal interests conflicted with those of his client. FF 19.

Thus undeterred, Respondent advised Ms. Fitzgerald to sign a confessed judgment in favor of the Condominium Association in the original principal amount of $17,000. FF 22.

By January 2013, while still representing Ms. Fitzgerald, Respondent had a "very acrimonious" discussion with her, during which she insisted that Respondent resolve the unpaid assessments or she would sell the condominium unit herself. FF 24. Despite the fact Ms. Fitzgerald was "yelling and screaming" at him about his unpaid obligations, Respondent did not move to withdraw from her representation, nor did he advise her to seek the advice of independent counsel about his continued representation of her. *Id.*

Instead, Respondent filed a separate but related civil action against his client. On August 16, 2013 (while still representing her in the Condominium Association suit), Respondent filed a declaratory judgment action against Ms. Fitzgerald claiming that he was the actual owner of the condominium unit. FF 25. She hired separate counsel, who filed an answer that denied Respondent's allegations and asserted a counterclaim seeking damages based on Respondent's breach of his agreement to pay for the mortgage and condominium fees. FF 30.

Respondent moved to withdraw from his representation of Ms. Fitzgerald on August 22, 2013, but, due to the motion's noncompliance with D.C. Super. Ct. Civ. R. 101(c)(2), his motion was denied without prejudice on November 20, 2013. FF 28-29. Respondent did not refile a compliant motion to withdraw until April 29, 2014 – more than five months later. FF 33. In the interim, he appeared as Ms. Fitzgerald's counsel at a status conference to discuss settlement of the Condominium Association's suit. FF 32. He remained her counsel in the Condominium litigation until May 6, 2014. FF 34.

The record evidence conclusively supports the Hearing Committee's factual findings concerning both the conflict in Respondent's representation of Ms. Fitzgerald and the absence of her informed consent. Respondent's personal interests were plainly adverse to those of his client, yet he failed to advise her of "the material risks of and reasonably available alternatives" to a conflicted representation. *See* Rule 1.0(e); *In re James*, 452 A.2d 163, 167 (D.C. 1982) ("'Full disclosure' includes a clear explanation of the differing interests involved in the transaction and the advantages of seeking independent legal advice."). Respondent "had an immediate conflict of interest because, at a minimum, [Ms. Fitzgerald] had a likely third-party claim against him. . . . Any competent, objective, independent attorney would have advised her of that fact . . . ." HC Rpt. at 60.

Indeed, it is evident that even with the most fulsome of disclosures, Ms. Fitzgerald could not properly have waived Respondent's conflict with her. Respondent was subject to a third-party claim by Ms. Fitzgerald in the Condominium litigation for all the damages the Condominium Association sought from her. *See* FF 18, 20. On this record, Respondent simply could not have "reasonably believed" that he could provide her with competent and diligent representation, since his own interests were irretrievably adverse to hers with respect to the core issues in the lawsuit. *See* Rule 1.7(c)(2) (Even with a client's consent, a lawyer may represent a client with respect to a matter only if the "lawyer *reasonably believes* that the lawyer *will be able to provide competent and diligent representation* to [the] client.") (emphasis added); Rule 1.7, cmt. [30] ("[I]t is doubtful that a lawyer

could hold such a belief . . . where the lawyer's individual interests make it likely that the lawyer will be adversely situated to the client with respect to the subject-matter of the legal representation."); *see* Restatement (Third) of the Law Governing Lawyers § 122 at 276 (2000); Geoffrey C. Hazard, Jr., W. William Hodes & Peter R. Jarvis, *The Law of Lawyering* § 12.31 (4th ed. 2015). Indeed, Ms. Fitzgerald ultimately recovered a judgment on her counterclaim against Respondent in the companion litigation; that judgment remained unsatisfied at the time of the disciplinary hearing, while the confessed judgment against Ms. Fitzgerald had grown to over $60,000 and had "destroyed" her credit rating. FF 39. Respondent's argument to the Board that he acted appropriately because he did not charge Ms. Fitzgerald for the legal representation, and that her "informed consent" was properly inferred from her status as "an informed, intelligent" mortgage broker (*see* Respondent's Brief ("R. Br.") at 7) thus completely misses the mark.

Finally, although we agree with the Hearing Committee that Respondent violated Rule 1.7(b)(4), we note that it erroneously stated that Respondent "bears the burden of proof that informed consent was secured." HC Rpt. at 60 (quoting Rule 1.7, cmt. [28]). While a respondent has the burden to *produce* evidence of informed consent, Disciplinary Counsel retains the *persuasion* burden of proof. *In re Szymkowicz*, Bar Docket Nos. 2005-D179 *et al.*, at 6 (BPR May 19, 2017) (emphasis added), *pending review*, D.C. App. No. 14-BG-884 (argued Apr. 11, 2018). Here, Disciplinary Counsel clearly and convincingly met that burden.

B. Count III: Reckless Misappropriation of Entrusted Funds (Mack)

Respondent undertook (as successor counsel) the representation of John Mack in a personal injury action. FF 112. At the time, Respondent knew that Kaiser Permanente had a $554 lien for medical services that it had provided to Mr. Mack in connection with his injuries. FF 113.

The Mack case settled, and on June 8, 2010 Respondent deposited the $9,000 settlement amount into his trust account. FF 114. He then appropriately disbursed all but $1,000, which he retained in escrow to pay the Kaiser Permanente claim. *Id.* Nine months later, on March 15, 2011, Respondent sought his client's permission to pay $554 to Kaiser Permanente. *See* FF 115.

Despite being aware of the amount of Kaiser Permanente's lien, Respondent allowed his trust account to fall below $554 as of April 22, 2011. *See* FF 116-117 (balance of $490.12). Thus, when Respondent wrote the $554 check to Kaiser Permanente on May 6, 2011, the account balance remained below the required amount. FF 118. In addition, five days later (on May 11, 2011), Respondent paid his office rent with another check, for $2,737.23, drawn on the trust account. FF 119. The latter check resulted in a negative balance of $2,247.11, until it was dishonored by the bank due to insufficient funds. *Id.* Once dishonored, the balance of the trust account rebounded to $460.12 (the original $490.12, less $30 for an "insufficient funds" checking fee). FF 120. There were insufficient funds in the trust account to cover the Kaiser Permanente obligation until May 12, 2011, when Respondent transferred $500 from his personal bank account to his trust account. FF 121, 123.

During his hearing testimony, Respondent admitted that he did not keep a ledger or similar record for his trust account and that maintenance of a ledger would have prevented him from depleting the trust account below the amount he was obligated to preserve for Kaiser Permanente. FF 122, 127. He also admitted that he knowingly deposited both personal and client funds into the trust account and paid personal expenses directly from it. FF 130; *see also* Respondent's Post-hearing Brief at 6 (conceding the failure to maintain records in Count IV); R. Br. at 13 (conceding the commingling of personal and client funds in Count IV). Among Respondent's personal deposits into trust were a mortgage refund, money from his mother, a check from his sister, a check from the sale of his automobile, a refund check from U.S. Airways, and a refund check from a boat repair. Respondent also acknowledged issuing several checks, payments, or wire transfers from the trust account that were of an obviously personal nature: payments to Ms. Fitzgerald, to a wine shop, to a diamond store, to a medical tourism company, and multiple payments to American Express. *See* Appendix to HC Rpt. (Chronological List of Trust Account Transactions); Specification of Charges, ¶¶ 25-26; Amended Answer, ¶¶ 25-26.

The Hearing Committee properly concluded that Respondent's commingling of client-related funds with his own personal funds "was not an inadvertent or isolated occurrence [but] was protracted, and took place throughout" a period of at least five years. FF 125. The Committee documented that Respondent commingled approximately $40,000 of non-client funds with client funds and paid approximately

$100,000 of his personal expenses from the trust account. FF 131. While Respondent claims that those expenses represented his fees, he paid various personal bills by indiscriminately making withdrawals without any ability to reconcile them with fees owed. *See* Appendix to HC Rpt., ¶¶ 2-6, 8-10, 12, 17, 28-31, 36, 38, 39, 41.

Misappropriation occurs when "the balance in the attorney's [trust] account falls below the amount due . . . regardless of whether the attorney acted with improper intent." *In re Edwards*, 990 A.2d 501, 518 (D.C. 2010) (appended Board Report). Therefore "when the balance in [a] [r]espondent's escrow account dip[s] below the amount owed[,]" misappropriation has occurred. *In re Chang*, 694 A.2d 877, 880 (D.C. 1997) (per curiam) (appended Board Report) (citing *In re Pels*, 653 A.2d 388, 394 (D.C. 1995)). There is no question that Respondent committed misappropriation. We must assess whether the misappropriation was reckless, or merely negligent.

Negligent misappropriation is characterized by "a good-faith, genuine, or sincere but erroneous belief that entrusted funds have properly been paid; and an honest or inadvertent but mistaken belief that entrusted funds have been properly safeguarded." *In re Abbey*, 169 A.3d 865, 872 (D.C. 2017). The hallmarks of recklessness, on the other hand, include "the indiscriminate commingling of entrusted and personal funds; a complete failure to track settlement proceeds; total disregard of the status of accounts in which entrusted funds were placed, resulting in a repeated overdraft condition; the indiscriminate movement of monies between accounts; and the disregard of inquiries concerning the status of funds." *In re*

Anderson, 778 A.3d 330, 338 (D.C. 2001). Writing checks that are dishonored or that cause a trust account to be in overdraft evidences recklessness, *see id*. at 340, as does the failure to reconcile a trust account or to maintain contemporaneous records of the flow and disposition of entrusted funds. *See, e.g.*, *Abbey*, 169 A.3d at 873-75; *Pels*, 653 A.2d at 396.

The Hearing Committee correctly concluded that Respondent engaged in reckless misappropriation. The "central issue" in determining the character of a misappropriation is whether the respondent handled entrusted funds "in a way that suggests the unauthorized use was inadvertent . . . or in a way that reveals either an intent to treat the funds as the attorney's own or a conscious indifference to the consequences of his behavior for the security of the funds." *Anderson*, 778 A.2d at 339. Engaging "in a pattern or course of conduct demonstrating an unacceptable disregard for the welfare of the entrusted funds" is sufficient to prove recklessness. *Id.*; *see also In re Hines*, 482 A.2d 378, 380 (D.C. 1984) (per curiam) ("reckless disregard" for the status of an account). While recklessness cannot be shown by inadequate record-keeping combined with commingling and misappropriation, *see Anderson*, 778 A.2d at 340, Respondent failed to maintain *any* meaningful records, wrote checks based on insufficient funds, and made no effort to reconcile the trust account. *See* HC Rpt. at 72 (citing *Anderson*, 778 A.2d at 340 and *Abbey*, 169 A.3d at 873-75), 85. He simply did not care enough to distinguish in any meaningful way between entrusted and non-entrusted funds and could not determine what client funds he held in trust at any given time or identify to whom they belonged. Hearing

Transcript ("Tr.") 280-81.[3] For years he casually and carelessly treated the trust account, and the funds in it, as his own. It is no surprise, therefore, that the account was overdrawn and that his rent check was returned for insufficient funds.

We agree with the Hearing Committee that Respondent "neither knew, nor cared, how much money was in his trust account or whether the monies were being properly held in a fiduciary manner." HC Rpt. at 85. It was no surprise that he committed misappropriation. Respondent's deliberately indifferent misappropriation was reckless. *See, e.g.*, *In re Pleshaw*, 2 A.3d 169, 173 (D.C. 2010); *In re Micheel*, 610 A.2d 231, 236 (D.C. 1992).

For that, Respondent must be disbarred. Kaiser Permanente was ultimately paid, and Mr. Mack was not harmed by the reckless misappropriation, but neither of those mitigating factors are of the "extraordinary kind" that can overcome the strong presumption of disbarment described in *Addams.* *See Micheel*, 610 A.2d at 237 n.14.[4]

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[3] Because he did not keep any records of trust account transactions, Respondent could not identify the source of personal deposits to the trust account or the recipient of personal payments made from the trust account. *See, e.g.*, Amended Answer, ¶¶ 25(a), 25(f), 26(a), 26(h) (Respondent answering that he "lacks sufficient information to either admit or deny that the deposit was received from Martha Dailey [Respondent's mother]," "lacks sufficient knowledge or information to form a belief that the funds were received as part of the sale of a watch . . . ," "lacks sufficient information to either admit or deny that the funds were sent to Tabitha Fitzgerald," and "is without knowledge or information sufficient to form a belief as to the truth of the allegations [of two payments to Gilda Scott], including from review of bank records").

[4] We also adopt the Hearing Committee's findings and conclusions concerning the violations of Rules 1.15(c) and (d) in the *Mack* matter. The Disbursement Statement created by Respondent, Disciplinary Counsel's Exhibit ("DX") 56, confirms that Respondent was aware of Kaiser Permanente's medical lien as early as June 8, 2010. Payment on that lien was not made, however, until the check cleared on May 23, 2011, almost a year after the settlement check was deposited into the trust account. FF 123; *see In re Nave*, Board Docket No. 12-BD-091, at 11 (BPR June 23,

C. <u>Count II: Intentional Misappropriation (Lawsuit Financial)</u>

We now turn to the issues raised by the charges in the Lawsuit Financial matter.

1. <u>Facts</u>

LFC, a Utah business corporation, provides funding to plaintiffs and attorneys engaged in personal injury litigation. FF 43; DX 31. In April and July 2010, Respondent entered into two "Pending Litigation Purchase Agreements" pursuant to which LFC advanced him a total of $25,000, in exchange for which Respondent committed to pay LFC the lesser of $100,000 or 20 percent of his attorney's fees collected in specified contingency fee cases. FF 44-45. The Agreements also gave LFC an aggregate $100,000 lien against Respondent's fees in those cases. *Id.* The arrangements were "non-recourse," meaning that LFC would receive nothing if there were no attorney's fees, and that Respondent's clients had no exposure to LFC. FF 44, 49, 52.[5] LFC disclaimed any "control, input, influence, right or involvement of any kind" in the conduct of the lawsuits. DX 31, 32.

The Agreements provided that LFC was to wire transfer the $25,000 to Respondent's operating account. *See id.* The Agreements did not identify Respondent as an escrow agent, nor did they mandate that Respondent hold any amounts due to LFC in trust. *See id.* The Agreements required disputes to be

2016) (six-month delay sufficient, no bright-line test for what constitutes "prompt" payment), *recommendation adopted*, 180 A.3d 86, 90 (D.C. 2018) (per curiam).

[5] The Hearing Committee referred to the Agreements as "Loan" Agreements, but neither purports to be a "loan." Rather, the Agreements characterize the arrangement as a "sale" of a portion of Respondent's fees in the underlying litigations. *See* DX 31, 32, ¶¶ 4, 15.

resolved by arbitration, but did not address where disputed finds were to be maintained. *See id.*, ¶ 10. Mark Bello, the attorney-founder of LFC, testified that he thought Respondent would escrow funds if their ownership was disputed (FF 59(e)), but it appears he did not convey that expectation to Respondent. Tr. 103, 117.

One of the personal injury cases identified in both Agreements was *Hedgepeth v. Whitman Walker Clinic, et. al.*, then pending in the D.C. Court of Appeals. FF 41, 47; DX 31, 32. *Hedgepeth* was the only case among those listed in the Agreements that resulted in attorney's fees to Respondent. FF 57. On August 27, 2012, Respondent deposited the $390,000 *Hedgepeth* settlement check, payable jointly to Respondent and his client, into his trust account. FF 66. At least one-third of that amount was his contingency fee, which Respondent disbursed directly into his operating account. *Id.*

For months thereafter, Respondent was evasive and dissembling when Mr. Bello of LFC attempted to learn whether the case had settled and what Respondent's attorney's fees were. As the Hearing Committee found:

> Respondent, finding himself in difficult financial circumstances, intended to delay any payment to LFC out of his legal fee in *Hedgepeth* for as long as possible, in an apparent effort to get LFC to agree to repayment from the results of other cases and to keep and make use of all of the Hedgepeth fees for himself. . . . Respondent's stiff-arming LFC occurred when he was experiencing financial pressures after suffering "devastating" losses in his legal practice . . . - severe enough to prevent him from paying his basic housing expenses . . . and to cause him to write an insufficient funds office rent check on his Trust

Account.[6] … In short, Respondent needed to misappropriate the funds due LFC, and he did so.

HC Rpt. at 80-81 (record citations omitted). In December 2014, LFC commenced an arbitration against Respondent to recover what it claimed to be owed under the Agreements. FF 94. Eight months later the arbitration was suspended on account of Respondent's "obstructive tactics." FF 106. In November 2015, LFC sued Respondent in D.C. Superior Court. FF 107. Respondent sought to dismiss LFC's case, arguing that the agreements were unenforceable because they violated Rule 5.4(a) of the Rules of Professional Conduct, which prohibits sharing legal fees with non-lawyers. FF 108. His motion was denied, and in April 2017 Respondent and LFC entered into a "Judgment of Consent" whereby the court would rule on the amount owed under the Agreements. FF 110.

LFC claimed entitlement to a greater amount, but Respondent testified that he believed that he owed LFC only $32,000. FF 92(b). From November 2013 through June 2014, however, his trust account balance repeatedly fell below that amount, and at times even fell below the $25,000 amount LFC had advanced to him. FF 111.

2. Discussion

Disciplinary Counsel argues that the plain language of Rule 1.15 establishes Respondent's obligations to LFC under the Agreements because Respondent received his contingency fee "in connection with a representation" (of Mr. Hedgepeth) and LFC was a "third-party" that had a "just claim" to a portion of those

[6] *See* discussion *supra*, at 9 (rent check).

fees. *See* Brief of Disciplinary Counsel ("ODC Br.") at 13 ("The plain language of Rule 1.15 applies to the portion of the *Hedgepeth* funds Respondent had pledged to secure a loan, and against which he had provided a lien."). That argument is outwardly compelling.

Rule 1.15(a) provides that:

> A lawyer shall hold property of . . . third persons that is in the lawyer's possession in connection with a representation separate from the lawyer's own property. Funds of . . . third persons that are in the lawyer's possession (trust funds) shall be kept in one or more trust accounts maintained in accordance with paragraph (b).

Rule 1.15(c) requires a lawyer "promptly" to notify the third person "[u]pon receiving funds . . . in which a . . . third person has an interest" and "promptly" to "deliver to the . . . third person any funds or other property that the . . . third person is entitled to receive." Finally, Rule 1.15(d) provides that if a "dispute arises concerning the respective interests among persons claiming an interest in such property, the undisputed portion shall be distributed and the portion in dispute shall be kept separate by the lawyer until the dispute is resolved. Any funds in dispute shall be deposited in" an escrow account. An attorney has an obligation to retain funds in a range of situations "where ownership interests are claimed by both the lawyer's client and a third party." *See* D.C. Bar Ethics Op. 293 (Feb. 2000) (citing *In re Thomas*, 740 A.2d 538 (D.C. 1999)).

Here, as the Hearing Committee recognized, Respondent received the funds claimed by LFC in connection with a representation. LFC had purchased an interest in Respondent's contingent fee recovery in cases he was handling in his capacity as

an attorney admitted in the District of Columbia. The gross settlement amount was paid, jointly to Respondent and his client, in connection with a personal injury action pending in a District of Columbia court. When Respondent received the settlement check, he deposited the entire amount in his trust account. A portion of those funds was client money, and LFC had a just claim to part of the amount due Respondent as attorney's fees. Although Respondent disputed the amount of LFC's claim, he concededly owed it at least $32,000 under the Agreements, and he obstinately failed to maintain that amount in his trust account. That failure, as explained by the Hearing Committee, violated the literal mandate of Rule 1.15 and, without more, would seem to constitute an intentional misappropriation requiring Respondent's disbarment under the rubric of *Addams*. HC Rpt. at 78-80.

We do not believe, however, that the analysis can or should end there. Respondent concedes that he failed to escrow the funds owed to LFC, but contends that his business dispute with a commercial litigation-finance company was beyond the reach of Rule 1.15. *See* R. Br. at 8-13. His argument is far from fanciful.

Lawyers and law firms regularly engage in commercial transactions and, when they do, are subject to the ordinary rules of the marketplace. A lawyer who is claimed to be in default on a business loan need not escrow the amount in dispute, on pain of disbarment. The Agreements at issue in this case are commercial in nature. They did not affect any client's financial interests, but instead were a small

sample of a commercial litigation funding industry that has drawn sophisticated lenders distributing billions of dollars to bankroll a diverse range of lawsuits.[7]

Application of Rule 1.15 to litigation funding arrangements could affect many of those transactions, possibly disrupting them in unanticipated ways. We are unaware of any judicial or disciplinary decisions applying Rule 1.15 (or its equivalents) to such arrangements, and the parties have candidly conceded they are aware of none.[8] The Hearing Committee recognized as much, and attempted to circumscribe its application of the Rule to the specific circumstances presented here, and not to "every commercial debt dispute by a lawyer." HC Rpt. at 77. We question whether the Hearing Committee's conclusion was correct, for three fundamental reasons.

First, LFC – the "third person" with a just claim seemingly contemplated by Rule 1.15 – was asserting its claim directly against Respondent, not against or through his client. The client's financial interests were not at risk in the Agreements. Under those circumstances, the application of Rule 1.15 becomes less clear. The Court's Rule 1.15 misappropriation decisions have consistently emphasized the fundamental value underlying the Rule: protection of the *client's* interest and the

[7] *See, e.g.*, Maya Steinetz & Abigail C. Field, *A Model Litigation Finance Contract*, 99 Iowa L. Rev. 711 (2014); Nathan Hale, *Litigation Funding Isn't Just for the Little Guy Anymore*, Law360 (Apr. 20, 2018), https://www.law360.com/articles/1033681/litigation-funding-isn-t-just-for-the-little-guy-anymore; Robert Barton & Wendy Walker, *Alternative Litigation Finance, Part I: The Waiting Game—The Economics of a Fiduciary Litigation Practice*, Probate & Property Magazine, Vol. 29, No. 05 (Sept./Oct. 2015).

[8] Disciplinary Counsel acknowledges that Rule 1.15 has not previously been interpreted to require an attorney to escrow funds owed to an attorney's creditor but argues that the plain language is determinative. ODC Br. at 12.

attendant confidence of the public in the legal profession. *See, e.g.*, *In re Pierson*, 690 A.2d 941, 948 (D.C. 1997); *In re Dulansey*, 606 A.2d 189, 190 (D.C. 1992) (per curiam). As well, Comment 7 to Rule 1.15, refers to fee disputes between a lawyer and his client: "a lawyer may not hold funds to *coerce a client* into accepting the lawyer's contention." *See* Rule 1.15, cmt. [7] (emphasis added). Comment 8 to the Rule also suggests that it is concerned with client interests:

> Third parties, *such as a client's creditors*, may have just claims against funds or other property in a lawyer's custody. A lawyer may have a duty under applicable law to protect such third-party claims against wrongful interference by the client, and accordingly may refuse to surrender the property to the client. However, a lawyer should not unilaterally assume to arbitrate a dispute *between the client and the third party*.

Rule 1.15, cmt. [8] (emphasis added) (citing D.C. Bar Ethics Op. 293). In our view, the absence of any threat to a client's interests cuts against the application of Rule 1.15 to this case.

Second, the pertinence of misappropriation principles to the Agreements in this case seems less certain because the funds provided by LFC were not "entrusted" by LFC to Respondent as a fiduciary; rather, those funds were sent to him in his role akin to that of a commercial borrower. Misappropriation is defined as "any unauthorized use of [a] client's funds *entrusted* to [the lawyer], including not only stealing but also unauthorized temporary use for the lawyer's own purpose, whether or not [the lawyer] derives any personal gain or benefit therefrom." *Anderson*, 778 A.2d at 335 (internal quotation marks and citation omitted) (emphasis added). "There are, therefore, three elements of misappropriation: (1) that client funds were

entrusted to the attorney; (2) that the attorney used those funds for the attorney's own purposes; and (3) that such use was unauthorized." *In re Travers,* 764 A.2d 242, 250 (D.C. 2000).

The Agreements did not create an obligation on the part of Respondent to escrow or to hold funds "in trust," either in their operational or dispute resolution sections. By comparison, in *In re Minninberg*, 485 A.2d 149, 151 n.22 (D.C. 1984) (per curiam), the Court considered a loan agreement signed by the respondent in which his $25,000 future legal fee was to represent "collateral security for any and all liabilities and obligations" of the respondent. Notably, the respondent signed a formal assignment, in which he agreed that any fees received "*shall be held in trust* by the [respondent] as the property of the Bank and shall forthwith be delivered to the Bank . . . ." *Minninberg*, 485 A.2d at 151 n.22 (emphasis added). The Board found that it was a "dishonest conversion" (akin to an intentional misappropriation) because the assignment had created a "trust relationship" as opposed to a "debtor relationship" between respondent and the lender with respect to the money owed. *In re Mininberg*[9], Bar Docket No. 390-79 *et al.*, at 7-8 (BPR Jan. 3, 1984) (explicit terms of the assignment in the signed document "established a trust relationship with respect to any money received by Respondent in the case to which the assignment related . . ."). The Court agreed with the Board's analysis, finding that the respondent had "breached a trust where his obligations under the assignment clause

[9] The Board Report spelled the respondent's name as "Mininberg," while the Court used "Minninberg."

were concerned." *Minninberg*, 485 A.2d at 151. Similarly, in *In re Green*, although we found misappropriation where no client interests were at stake, we emphasized that the respondent had been specifically entrusted with funds because he had committed to hold them in escrow. Board Docket No. 13-BD-020, at 10 (BPR Aug. 5, 2015), *recommendation adopted*, 136 A.3d 699, 701 (D.C. 2016) (per curiam). Here, in contrast, by signing the two Agreements, Respondent was only a "'stakes-holder' . . . in a private commercial transaction." *In re Speights*, No. 17-BG-1091, slip op. at 7 (D.C. July 26, 2018) (citing *In re Confidential*, 664 A.2d 364, 367 (D.C. 1995)). He did not commit to act as a fiduciary of LFC. In our view, the absence of any escrow requirement also cuts against the application of Rule 1.15 to this case.

Finally, there are policy concerns that call into question the reasonableness of applying the concept of misappropriation to litigation funding arrangements. The Rules of Professional Conduct "are rules of reason. They should be interpreted with reference to the purposes of legal representation and of the law itself. . . ." *See* D.C. Rules of Prof'l Conduct: Scope [1]. In *In re Perrin*, 663 A.2d 517, 523 (D.C. 1995), the Court explained that when it considers the plain language of the Rules, it also considers the policy or purpose of the Rules as a whole, especially where the plain language would lead to an unreasonable result:

> Although this court subscribes to the familiar doctrine that the language of statutes (and rules) is to be accorded its ordinary meaning, *see, e.g.*, *James Parreco & Son v. District of Columbia Rental Hous. Comm'n*, 567 A.2d 43, 45-46 (D.C. 1989), "we must not . . . make a fetish out of plain meaning." *Id.* at 46. "Courts do not wallow in literalism where the plain language of a statute would lead to absurd consequences which the legislature could not have intended." *Id*. (citations omitted).

> "[E]ven when the plain meaning did not produce absurd results but merely an unreasonable one plainly at variance with the policy of the legislation as a whole, this [c]ourt has followed that purpose, rather than the literal words." *Id.* (quoting *United States v. American Trucking Ass'n*, 310 U.S. 534, 543, 60 S.Ct. 1050, 1064, 84 L.Ed. 1345 (1940)) (internal quotation marks omitted).

Perrin, 663 A.2d at 523. In *In re Clower*, 831 A.2d 1030, 1034 (D.C. 2003) (per curiam), the Court similarly agreed with the Board that the Rules "should be interpreted with reference to their purposes." Layering the misappropriation concept onto the commercial litigation funding marketplace would seem to expand the application of Rule 1.15 well beyond its fundamental purpose, the protection of clients' interests.

In that regard, we cannot blind ourselves to the sanction applicable were we to find misappropriation here. In *Addams* and its progeny, the Court emphasized that severe sanctions are imposed in Rule 1.15 misappropriation cases, because misappropriation '"strike[s] at the core of the attorney-client relationship' by undermining the public's faith that attorneys will fulfill their duties as fiduciaries in handling funds entrusted to them by their clients." *Pierson*, 690 A.2d at 948 (quoting *Addams*, 579 A.2d at 198-99); *see also Dulansey*, 606 A.2d at 190. Whether the stark threat of disbarment should hover over attorneys who enter into commercial litigation funding agreements where, as here, no client funds are at risk is also a serious question.

All of these difficult and subtle issues present themselves in the context of an industry that is itself in flux and of concern to courts, legislatures, and disciplinary

authorities.[10] Moreover, although ethics opinions in some states have approved such arrangements under certain conditions (*see, e.g.*, New York, Florida, Nevada, New Jersey, South Carolina, and North Carolina[11]), others have prohibited them (*see, e.g.*, Maine, Utah, Michigan, Ohio, and Virginia[12]). Neither the substantive legality nor

[10] *See, e.g.*, Proposed Revision of Civil Local Rule 3-15, Standing Order for all Judges of the Northern District of California (Jan. 17, 2017) (adding to "Certification of Non-party Interested Entities or Persons" required by Civil Local Rule 3-15 to include the required disclosure of "any person or entity that is funding the prosecution of any claim or counterclaim"); Wisconsin Act 235, 2017-2018 Wisc. Legis. Serv. Act 235 (West) (Apr. 3, 2018) (litigation funding agreements are to be disclosed in civil actions in Wisconsin state courts); Litigation Funding Transparency Act of 2018, S. 2815, 115th Cong. (2018) (legislation introduced on May 10, 2018 by Senate Judiciary Committee Chairman Chuck Grassley and Senators Thom Tillis and John Cornyn which requires the disclosure of third-party litigation financing agreements in civil lawsuits).

[11] *See* N.Y. State Bar Assoc. Ethics Op. 666 (June 3, 1994), Op. 769 (Nov. 4, 2003), and Op. 1108 (Nov. 15, 2016) (client confidences must be maintained, the lawyer must not own an interest in the finance company and may not receive a referral fee, and the transaction must not be illegal or violate usury laws); Fla. Bar Ethics Op. 00-3 (Mar. 15, 2002) (lawyer may provide client with information about third-party litigation financing if lawyer believes it is in the client's best interest); State Bar of Nevada Standing Comm. on Ethics and Prof'l Responsibility, Formal Op. 29 (Aug. 7, 2003) (lawyer may refer clients to litigation finance company so long as the lawyer owns no interest in the company and client consents after consultation); N.C. State Bar 2006 Formal Ethics Op. 12 (Oct. 20, 2006) (lawyer can use part of his contingent fee as collateral for a non-recourse loan with a litigation funding company, but client must give informed consent because "nature and value of a case certainly is client confidential information"); S.C. Bar Ethics Advisory Op. 92-06 (1992) (an attorney may own interest in a non-recourse financing company that provides funding to non-clients); Bar Ass'n of the City of N.Y. Comm. on Prof'l Ethics Formal Op. 2011-2 (June 1, 2011) (not unethical *per se* for lawyers to advise a client on or be involved in third-party litigation financing agreement but lawyers must be prepared to address ethical issues of potential waiver of privilege and conflicts in interest); N.J. Advisory Comm. on Prof'l Ethics Op. 691 (2001) (permitted so long as attorney advises client of potential loss of attorney-client privilege that will result from disclosures to financing companies).

[12] *See* Bar of Maine Prof'l Ethics Commission, Op. 193 (Dec. 10, 2007) (non-recourse loan to finance litigation in a contingency fee case not permitted because the agreement constitutes the sharing of legal fees with a non-lawyer); Utah State Bar Op. 06-03 (2006) (attorney may not ethically participate in contingent, non-recourse litigation funding due to inherent conflict in interest); State Bar of Mich. Op. RI-321 (2000) ("depths of conflicts of interest" make client's consent or waiver unattainable); Ohio Supreme Court Bd. of Comm'rs on Grievances and Discipline, Advisory Op. 2004-2 (2004) (lawyer may not agree to give a litigation finance company a share or security interest of his contingency fee); Virginia Legal Ethics Op. 1764 (2002)

the ethical propriety of such arrangements has yet been addressed in the District of Columbia.

For all of these reasons, we conclude that the propriety of applying Rule 1.15 to the litigation funding agreements in this case – which purport to be governed by Utah law – would be imprudent, since the resolution of that thorny question would not affect our recommended sanction. *See, e.g.*, *Travers*, 764 A.2d at 250 (leaving resolution of an issue for a future case where case law "sparse and inconclusive"). Respondent committed reckless misappropriation in the Mack matter and, for that reason, must be disbarred.

SANCTION

For the reasons set forth *supra* and in the Ad Hoc Hearing Committee's Report and Recommendation, we recommend that Respondent be disbarred for his reckless misappropriation in the Mack matter (Count III), the sanction mandated by *Addams*. We further recommend that the period of disbarment run for purposes of reinstatement from the filing of the affidavit required by D.C. Bar R. XI, § 14(g). *See In re Slosberg*, 650 A.2d 1329, 1331-33 (D.C. 1994).

BOARD ON PROFESSIONAL RESPONSIBILITY

By: ________________________________
Robert C. Bernius

All members of the Board concur in this Report and Recommendation.

(attorney may not share a portion of a contingent fee with a litigation finance company because it violates rule against sharing of fees with a nonlawyer); Virginia Legal Ethics Op. 1155 (1988) (lawyer cannot co-sign or act as guarantor for litigation funding agreement).